

## Message Text

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SUBJECT: INR ASSESSMENT OF VENEZUELA'S NEW RULES FOR FOREIGN INVESTORS

FOLLOWING ARE HIGHLIGHTS OF INR INTELLIGENCE NOTE, DATED MAY 21, "VENEZUELA: NEW RULES FOR FOREIGN INVESTORS":

1. PRESIDENT PEREZ'S NEW INVESTMENT POLICY--WHICH INCLUDES EARLY REVERSION TO VENEZUELA OF FOREIGN-HELD PETROLEUM CONCESSIONS--MAY PROVE, IN ITS IMPLEMENTATION, TO BE MORE MODERATE AND LESS ONEROUS TO FOREIGN INVESTORS THAN IT MIGHT INITIALLY APPEAR. ESSENTIALLY, HE IS BRINGING VENEZUELA INTO LINE WITH OTHER LATIN AMERICAN COUNTRIES IN WHICH STATE OIL AND MINERAL CONTROLS, INSISTENCE ON JOINT VENTURES, AND LIMITATIONS ON FOREIGNERS IN UTILITY, MEDIA, AND PROFESSIONAL SERVICES ARE THE RULE (E.G., MEXICO AND BRAZIL).
2. PEREZ'S NOT-UNEXPECTED MAY 16 ANNOUNCEMENT CONCERNING THE OIL CONCESSIONS (WHOSE REVERSION WAS SCHEDULED TO BEGIN

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IN 1983) INDICATED THAT A SPECIAL COMMISSION IS TO MAKE

ACTION RECOMMENDATIONS AS SOON AS POSSIBLE. FOREIGN OIL COMPANIES WILL APPARENTLY CONTINUE TO PLAY AN IMPORTANT ROLE, BUT A PROPOSED NEW NATIONAL PETROLEUM AGENCY WILL EVENTUALLY TAKE OVER THEIR PHYSICAL ASSETS AND EXERCISE

CONTROL OVER THEIR OPERATIONS. TAKEN WITH OTHER RECENT MOVES AFFECTING FOREIGN INVESTORS, PEREZ'S ANNOUNCEMENT ESTABLISHES THAT HIS ADMINISTRATION FULLY INTENDS TO:

(A)--USE ITS OIL INCOME BONANZA TO EXTEND THE ROLE OF THE STATE IN PETROLEUM AND OTHER BASIC INDUSTRIES;

(B)--EXPLOIT THE WORLD'S PRESUMED NEED FOR VENEZUELA'S RAW MATERIALS TO FORCE NEW TERMS ON MULTINATIONAL OIL AND MINING COMPANIES; AND

(C)--BRING UNDER VENEZUELAN SUPERVISION AND AT LEAST PARTIAL OWNERSHIP MANY OF THE OTHER FOREIGN-OWNED COMPANIES OPERATING IN VENEZUELA.

3. OTHER INITIATIVES: SINCE APRIL 29 PEREZ HAS ANNOUNCED:

(A)--PLANS TO RENEGOTIATE TERMS ON WHICH FOREIGN IRON-MINING COMPANIES, NAMELY US STEEL AND BETHLEHEM, AND JAPANESE AND US (REYNOLDS) ALUMINUM INVESTORS WILL BE ALLOWED TO OPERATE; AND

(B)--NEW DECREES IMPLEMENTING THE ANDEAN FOREIGN INVESTMENT CODE, UNDER WHICH FOREIGN-OWNED SERVICE ENTERPRISES MUST SELL OFF 80 PERCENT OF THEIR EQUITY TO VENEZUELAN INVESTORS WITHIN THREE YEARS.

4. WHILE PEREZ'S POLICIES WILL SERIOUSLY AFFECT MANY US INVESTORS--WHOSE TOTAL INVESTMENT STAKE IN VENEZUELA IS ABOUT \$2.7 BILLION (BOOK VALUE AT END OF 1972)--HIS PROGRAM DOES NOT NECESSARILY IMPLY EXPROPRIATION A LA PERU OR BOLIVIA IN THE LATE 1960S. EXISTING CAPITAL IN MANUFACTURING (MORE THAN \$500 MILLION BOOK VALUE) DOES NOT APPEAR TO BE AFFECTED DIRECTLY. RATHER, PEREZ APPARENTLY INTENDS TO USE VENEZUELA'S SOUGHT-AFTER RAW MATERIALS  
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AND ADVANTAGEOUS MARKET POSITION TO PERSUADE FOREIGN INVESTORS IN THE EXTRACTIVE INDUSTRIES TO AGREE TO NEW RULES OF THE GAME. IF COMPANIES AFFECTED BY THE NEW MEASURES DO NOT ACCEPT HIS TERMS, PEREZ APPARENTLY BELIEVES THAT HE CAN GET WHAT HE WANTS FROM OTHER FIRMS OR BUY NEEDED TECHNOLOGY ON THE OPEN MARKET.

5. PEREZ SIGNALLED THE THRUST

OF HIS ECONOMIC POLICIES SOON AFTER THE ELECTION--BY A

SUBSTANTIAL MARGIN--OF HIS REFORM-MINDED SOCIAL DEMOCRATIC ADMINISTRATION LAST DECEMBER. HIS POLICIES CONSTITUTE THE UNDERPINNING FOR A WIDE-RANGING ECONOMIC AND SOCIAL ACTION PROGRAM TO WHICH HE HAS COMMITTED HIS GOVERNMENT AND FOR WHICH HE HAS BROAD POLITICAL AND POPULAR SUPPORT. HIS POLICIES, IN FACT, CARRY FORWARD INITIATIVES FORESHADOWED BY THE CHRISTIAN DEMOCRAT ADMINISTRATION HE REPLACED.

6. PEREZ'S LEGISLATURE WILL NEED TIME TO ENACT HIS PROGRAM. MOREOVER, IMPLEMENTATION OF HIS NEW FOREIGN INVESTMENT POLICY WILL TAX THE ADMINISTRATIVE AND FINANCIAL MANAGEMENT CAPABILITIES OF HIS GOVERNMENT. THE FORCED SELL-OFF OF SERVICE COMPANY EQUITY TO NATIONAL INVESTORS WILL REQUIRE NEW AND IMPROVED CAPITAL MARKET MECHANISMS. IRON AND ALUMINUM INVESTORS CAN LOOK FORWARD TO DRAWN-OUT BARGAINING. AND, AS PEREZ ADMITS, NO STUDY YET EXISTS OF THE MULTIPLE ASPECTS INVOLVED IN HIS OIL-REVERSION PROGRAM.

7. US COMPANY OFFICIALS IN VENEZUELA HAVE TENDED SO FAR TO TAKE A "WAIT-AND-SEE ATTITUDE. COMPENSATION IS NOT LIKELY TO BECOME A MAJOR ISSUE IN ANY EVENT, GIVEN VENEZUELA'S WEALTH AND COMMITMENT TO PAY FOR ANY PROPERTIES EVENTUALLY NATIONALIZED. BUT PAYMENT COULD BE ON A MINIMUM BASIS: PEREZ HAS STATED THAT PETROLEUM COMPANY ASSETS--\$1.5 BILLION IN BOOK VALUE IN 1972--WILL BE TAKEN OVER AT NET BOOK VALUE.

8. OUTLOOK: THE PROSPECTIVE REORDERING OF VENEZUELA'S RELATIONSHIPS WITH FOREIGN INVESTORS IN THE RESOURCE SECTOR WILL TEST ITS BARGAINING POWER IN THE WORLD ECO-  
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NOMIC ARENA. THE SUCCESS OF PEREZ'S POLICIES WILL DEPEND UPON THE EXTENT TO WHICH:

(A)--WORLD DEMAND FOR VENEZUELA'S OIL, IRON, AND ALUMINUM PRODUCING CAPACITY PERSUADES THE MULTINATIONAL COMPANIES TO ACCEPT HIS TERMS;

(B)--VENEZUELA IS SUPPORTED BY OTHER IRON-ORE AND BAUXITE-PRODUCING COUNTRIES; AND

(C)--THE STATE IS ABLE TO ASSURE CONTINUED INVESTMENT IN PETROLEUM, INCLUDING THE ORINOCO OIL BELT. RUSH

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